United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

BPIs

74-1533

To be argued by
LOUIS P. ROSENBERG

United States Court of Appeals
FOR THE SECOND CIRCUIT

In the Matter of

SAPPHIRE STEAMSHIP LINES, INC.,

Bankrupt-Appellant,

and

J. READ SMITH,

Trustee-Appellant,

—against—

WINTHROP, STIMSON, PUTNAM & ROBERTS, ATTORNEYS FOR E. BERGENDAHL CO., INC. (NEW YORK) AND E. BERGENDAHL CO., INC. (PHILADELPHIA), CREDITORS,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF ON BEHALF OF TRUSTEE-APPELLANT

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Statement

This is an appeal from only so much of the Opinion and Order of Hon. Milton Pollack, District Judge, dated March 15, 1974 (77-a)* which rejected the recommendation of Asa S. Herzog, Bankruptcy Judge, set forth in the Certificate of Allowances dated February 8, 1974 (63-a) to

* Numbers in parentheses preceded by letter "A" refers to Appellant's Appendix.

deny the allowance application of the appellees as attorneys for two creditors on the ground "that absent an order of the court authorizing his employment, an attorney who renders services to the trustee or for the benefit of the estate is a volunteer who may not be paid from the estate" (71-a).

In rejecting the recommendation, the Court remanded to the Bankruptcy Court to consider the fair and reasonable value of the services allegedly rendered by appellees in contributing to the creation of the fund, being the proceeds realized by the trustee in the settlement of the antitrust action.

Issue

The trustee herein retained skilled special counsel pursuant to order of the Court and was ably represented throughout the prosecution of the antitrust action until final settlement, should counsel for two creditors be compensated for unsolicited and unauthorized services which, it is alleged, contributed to the ultimate settlement of the law suit?

Facts

The facts are fully recited in the Certificate of Allowance by Bankruptcy Judge Asa S. Herzog (63-a) and in the opinion rendered by the Court below by District Judge Milton Pollack (77-a).

In substance the trustee retained Joseph L. Alioto, Esq. as special counsel, pursuant to order of November 8, 1967, to prosecute a civil antitrust suit to recover damages resulting from the acts of the defendants. During the course of

that action, counsel negotiated a tentative compromise of the litigation for the sum of $1,600,000.

As required by the provisions of the Bankruptcy Act (58(6)), a hearing was held for the consideration of said offer. The appellees, representing two creditors, appeared in opposition to acceptance of the offer. However, the court approved the offer but on reargument, in which appellees joined with the United States Attorney, the Bankruptcy Judge reversed his "original stand" and disapproved this offer "primarily because I was impressed with the evidence produced by the Internal Revenue Agents who were put to work on the case by the Government". (70-a)

Appellees admit in their memorandum in support of their application for attorney's fee (Exhibit 7) that the attorneys for the trustee negotiated a second offer of settlement with the defendants in the pending litigation for the sum of $2,473,070.12 of which fact the appellees were "not informed until later" (Exhibit 7, p. 35). Mr. Reilly, the then Assistant U.S. Attorney approved said second offer which was thereafter approved by the Bankruptcy Judge notwithstanding continued opposition by the appellees, on behalf of creditors.

There is no suggestion or claim by the appellees that they assisted the attorneys for the trustee in the prosecution of the pending antitrust litigation or in negotating either the first or second offer of settlement. Their sole position was that as attorneys, for their two clients, they acted in cooperation with the Attorney General's Office in opposition to the first offer of settlement, and even though the Assistant U.S. Attorney, confirmed to the appellees that "the Attorney General's office had approved the subsequent settlement" of $2,473,070.12, the appellees continued to oppose

the settlement which was approved by the Bankruptcy Judge, (Exhibit 7, pp. 37-39).

The Bankruptcy Judge, without even scheduling a meeting of the creditors, filed his report recommending the denial of any compensation on the theory that "what they did, they did for their clients"; also that the trustee was represented by counsel retained pursuant to Order of the Court whereas the appellees had not been retained or their assistance sought by the trustee nor was there a Retention Order entered in accordance with General Order 44.

In the light of these facts and the settled law enunciated by this Court, the Bankruptcy Judge correctly concluded that appellees could not be compensated from this estate.

POINT I

The Bankruptcy Act does not allow compensation to attorneys for creditors when the trustee and his counsel are functioning.

Appellant, as Trustee in Bankruptcy, retained Louis P. Rosenberg, as attorney pursuant to an Order of this Court and also pursuant to Order of the Court retained Joseph L. Alioto, as special counsel to prosecute the antitrust suit. The said action was prosecuted capably and diligently by experienced counsel.

Appellees only status in this proceeding is as attorneys for two creditors. They performed no services in the antitrust case itself. Indeed, they make no claim that they did. Their memorandum in support of their application for attorneys' fees sets forth the services rendered and the time spent. All of it has to do with their opposition to the original settlement which was disapproved and to the later settlement which was approved, despite their opposition.

Subsequent to the rejection of the first offer of settlement, a new motion for summary judgment was prepared and filed, and opposition to defendants' counter-motion for summary judgment was prepared and filed. The entire burden of carrying on the antitrust case, both before and after the disapproval of the $1,600,000. settlement, was borne by Special Counsel and his associates without any help from appellees representing the two creditors.

Nor did counsel for appellees bring about an increase in the settlement from $1,600,000. to $2,447,000. That was accomplished as a result of negotiations between Special Counsel and counsel for the defendants. At their joint request, counsel for the Government agreed to submit the case to the antitrust division of the Department of Justice for an evaluation of the merits of the then pending settlement proposal. Following this evaluation, the Attorney General gave his approval to the proposed settlement and stated that, in his opinion, it was fair and reasonable. Thereafter the renegotiated offer was submitted to the Court for consideration. Appellees were just as vigorous in their opposition to this offer as they were to the original offer.

Thus, it cannot be said that appellees were responsible for the creation of a fund from which other creditors benefited. The most that they did was to oppose, along with numerous other creditors, the first offer. But such disapproval created no fund. The antitrust case went back on the trial calendar. The fund was created by the second offer in which appellees not only had no part, but which they vigorously opposed. Had they had their way there would even now be no fund for distribution to the creditors. Hence, on the facts the cases relied upon by Judge Herzog are clearly right. Appellees' services benefited their cli-

ents as did the services of counsel for the other creditors who appeared in opposition to the first settlement benefit their clients. They should look to their clients for compensation and not to the bankrupt estate.

In referring to appellees status and activities in this proceeding, Judge Herzog observed:

> "But more important, Winthrop, Stimson, Putnam & Roberts appeared on behalf of two creditors, they appear as such on the record. *At no time were they acting as attorneys or special attorneys to the trustee, nor was any order made authorizing them to act for the trustee in any capacity whatsoever.* What they did, they did for their clients; their clients will reap the benefit of their services; they must look to their clients for payment."
>
> "It could pave the way to grave abuse, if without being authorized to act by the court, counsel for creditors could look to estates for compensation because in the process of representing and protecting their clients, the estate was incidently enhanced."
>
> "It is for precisely that reason that General Order 44 was promulgated by the Supreme Court:"
>
> "No attorney for a receiver, trustee or debtor in possession shall be appointed except upon order of the court, which shall be granted only upon the verified petition of the receiver, trustee or debtor in possession."
>
> "This mandate has been carried over into the new Bankruptcy Rules. Rule 215(a) providing:"

> "No attorney or accountant for the trustee or receiver shall be employed except upon order of the court. . . ."

The court also cited and quoted extensively from *In Re Siegel* (S.D.N.Y.) where Judge Learned Hand:

> "Any services rendered by those not authorized by the receiver must be deemed to be on the account of the creditors who undertake them. They are merely volunteered and the estate, even though actually benefited, owes nothing for them. There is no hardship in this, but absolute justice."

And in *Sartorious* v. *Bardo* 95 F. 387 (2d Cir.) where Judge Hand again denied compensation to a volunteer:

> "The services of those who choose to help him in these duties, even at his invitation, will be treated as rendered in their several interests alone and not for the estate, unless they present to the court in advance their pretension to represent it, showing some reason why the trustee's unaided efforts will not serve. If the court then recognizes them, they become trustees *pro hac vice* and can be paid; not otherwise. (citing cases)."

The recommendation for denial of compensation to the appellees was proper in light of the consistent rulings of this Court.

POINT II

The decision and order under appeal is inconsistent with decisions of this Court denying compensation to a volunteer even for beneficial services.

The decision of the District Judge is predicated on a concept that beneficial services should be rewarded.

> "It appears that the Bankruptcy Judge did not give effect to overriding equitable principles which are applicable to the special facts herein that require payment of compensation for services rendered for the benefit of all creditors as a class."

The Court proceeded on the theory that if the services were beneficial and contributed to the increased recovery, then there should be some measure of compensation. Without conceding that appellees' services were involved in the anti-trust litigation, but assuming arguendo, that it may have been considered in the subsequent negotiations for the increased offer, the benefit should not be attributed to appellees' efforts nor would same be compensable.

In a decision of this Court, *In re Progress Letkro Shave*, 117 F. 2d 602 (1941) compensation was denied to the attorney for the bankrupt who had rendered benefical services for the trustee "with the consent and approval of the referee" because the trustee is the sole administrator of the estate and no one may act for him directly or indirectly without formal authorization of the Court. The remarks of the Court are apposite.

> "The services rendered were not a duplication of the work of any other attorney, nor is there any ques-

tion that some of them were beneficial to the estate and its administration. Further, no one suggests that $3,000. is not a reasonable sum; in fact it appears to be a very moderate charge for the time and labor expended; the basis for the denial of the allowance by the district court was that the bulk of the appellant's service was of a character to be rendered by an attorney for the trustee and the appellant had not been appointed to serve in that capacity, as required by General Order 44, 11 U.S.C.A. following section 53; nor would he have been eligible for such appointment because not "disinterested" as required by Sections 157 and 158 of the Chandler Act. 11 U.S.C.A. Sections 557, 558."

"There is no question but that the appellant acted throughout in good faith and a denial to him of compensation is a harsh conclusion. However, the law is unquestionably settled that the order of the district court was correct. In the case of in re Eureka Upholstering Co., 2 Cir. 48 F. 2d 95 the attorney for the petitioning creditors rendered valuable services to the receiver in bankruptcy; it was held, however, that having failed to secure formal appointment under General Order 44 no compensation could be recovered irrespective of benefit to estate. A similar ruling appears in Re Rogers-Pyatt Schellac Co., 2 Cir., 51 F. 2d 988 and in Re H. L. Stratton, Inc., 2 Cir., 51 F. 2d 984, certiorari denied sub nom. Jonas & Neurburger v. General Motors Acc. Corp., 284 U.S. 682, 52 S. Ct. 199, 76 L. Ed. 576. See also Weil v. Neary, 278 U.S. 160, 49 St.Ct. 144, 73 L. Ed. 243; In re Robertson, 3 Cir., 4 F. 2d 248. To recover compensation from the estate for

services rendered to the trustee an attorney must receive appointment under General Order 44."

"It is true that the appellant acted throughout with the consent and approval of the referee, but this does not bring him within the proviso of section 157, 11 US.C.A. Section 557. The waiver of disinterestedness there permitted must take the form of an appointment under General Order 44 and must be explicit; it can not take the form of silent acquiescence. See In re H.L. Stratton, Inc., 2 Cir., 51 F. 2d 984, 987; In re Giannini, D.C.S.D.N.Y., 14 F. Supp. 1005, 1007."

"Nor can compensation be allowed on the ground that the services were rendered in the capacity of attorney for the debtor and resulted in benefit to the estate. *A trustee having been appointed it was his duty to administer the estate and recovery can not be had by others unless the trustee refuses to act and formal authorization is procured from the court to proceed in his stead.* In re Porto Rican Am. Tobacco Co., supra. (Emphasis supplied)

Mindful of this Courts admonition that "volunteers" will not be compensated even if it results in a "harsh conclusion" the District Court relies on the equitable principle that where lawyers participate in class action and their services contribute to a recovery, they are entitled to compensation out of the funds "because those who accept the benefits of such services must also assume a share of the expenses connected therewith".

This theory is not applicable and has been rejected in bankruptcy proceedings. In *Guerin* v. *Weil & Gotshal* 205 F. 2d 302 (1956), this Court said: (304)

> "It is well settled that the bankruptcy court lacks power to grant, and the policy of the Act is against compensation not expressly provided for by the Act (citing). Although it has been broadly stated that a bankruptcy court is a court of equity, Young v. Higbee 324 U.S. 204, 214, the exercise of its equitable powers must be strictly confined within the prescribed limits of the Bankruptcy Act, see Berry v. Root 5 Cir, 148 F. 2d 945, 946, cert. den., where Congress intends that allowances should be made it has carefully enumerated them, and any omissions must be construed as express exclusion, 3 Colliers, Bankruptcy 1534-7 (14th Ed.)".

To the same effect is *Berry* v. *Root* (C.A. 5th) 148 F. 2d 945 where in holding that *Sprague* v. *Ticonic National Bank* 307 U.S. 161 (cited by Judge Pollack) is "not controlling in bankruptcy", remarked:

> "Much reliance is placed by appellants on Sprague v. Ticonic Nat. Bank, 307 U.S. 161, 59 S.Ct. 777, 83 L. Ed. 1184. The case is not applicable. There was no bankruptcy. The assets of the bank were in court through a receiver. Sprague successfully maintained the existence of a trust on certain assets to secure depositors like herself. She herself sought to have these other depositors contribute from the trust fund towards her costs and expenses in vindicating the common right. The decision was that a court of equity could entertain her application. We held this case not controlling in bankruptcy in Lea V. Patterson Savings Inst., 5 Cir., 142 F.2d 932."

The other authorities cited in the decision of the District Court did not involve bankruptcy proceedings or are readily

distinguishable. Randolph v. Scruggs 190 U.S. 533 allows compensation for services in preserving the estate *prior* to the appointment of the trustee.

Appellee relies heavily on the decision of this Court *In re New York Investors* 130 F. 2d 90 which concededly very limitly is an exception from the rigid requirements enunciated in *Sartorious v. Bardo*, *In re Progress Letkro Shave*, *Porto Rican Am. Tobacco Co.* and *Guerin v. Weil & Gotshal*, supra. However, the exception does not alter appellees' position because the court emphasized that the rule was being relaxed due to the unusual circumstances "that trustees cannot be expected to take appeals from their own allowances" and that the intervention by RFC required the rendition of services "such as the trustee cannot reasonably be expected to perform" (p. 92).

The Court simultaneously demonstrated that, but for this rare and unprecedented instance, it remained adamant in its policy of no allowance for unauthorized services, by denying compensation to RFC even when it successfully opposed the allowance to one, Edward Endelman, Esq., counsel for an intervening Creditors' Committee. It stated (p. 92):

> "It is said that the same reasoning should apply to Endelman's allowances because the trustees refused to appeal from the order allowing them, though they were requested by the RFC to do so. But there was nothing to prevent an application by the RFC to the court for an order directing the trustees to appeal (and they were apparently appropriate persons to do so) or authorizing the RFC to do so in their stead. Under such circumstances, we think an application was necessary before the RFC was entitled to claim any compensation from the estate for appealing Endelman's allowances."

Thus, it is plain the trustee is the sole administrator of a bankrupt estate and anyone seeking compensation for beneficial services allegedly rendered, even when the trustee declined to act, must first be authorized by Order of the Court.

In an apparent effort to overcome the absence of authorization, there appears the semblance of an inference that the trustee and counsel might not have been acting in the best interests of the estate. This is completely unfounded and irresponsible. Any suggestion reflecting on the good faith of counsel is obviously fashioned to create the impression that appellee had to participate in order to properly protect the interests of the estate. That situation did not exist. If appellees or their clients entertained any doubt of the trustee's sincerity in the prosecution of the antitrust suit or had lost confidence in special counsel's prosecution of the action, their remedy was to apply to the Court for appropriate relief—such as removal of the trustee, disqualification of counsel or even to be substituted as counsel to prosecute the antitrust action. (*In re New York Investors* supra 92). Significantly, they did nothing because there was no reason to do so.

Not having been retained by the trustee nor having procured an Order from this Court authorizing the rendering of services in furtherance of the estate, appellees' must be considered "volunteers" and are not entitled to compensation from the estate. The admonition of Judge Learned Hand (*In re David Siegel* 252 F. 197) that any services rendered by those not authorized by the receiver or trustee are merely volunteers and not entitled to compensation even where the services were beneficial has been consistently followed by this Court and in other jurisdictions, *In re Hydra*

Carbon 3rd Cir. (1969) 411 F. 2d 203; *Gochenour v. Cleveland Terminals* 6th Cir. 142 F.2d 991.

That courts will continue to protect bankrupt estates from volunteered assistance by overzealous attorneys is pointed out *In re Owl Drug Co.* 16 F. Supp. 319 aff'd sub nom, *Cohen v. Edler* C.A. 9th 90 F.2d 823, where it is said:

> "Were the law otherwise, there would be no limit to the burden which might be placed upon an estate if attorneys for the bankrupt or individual creditors could, by doing work which it is not their duty to do, by assisting the trustee, without an order of court allowing their special employment,—burden the estate with the added cost of performing work which it is the duty of others to perform. The bankruptcy court would lose control in the matter of fees. 'Volunteers' would be plentiful. And it is almost certain that in every estate of any size, the courts would be confronted with claims for 'voluntary' assistance."

The report of the Bankruptcy Judge is consistent with the decisions of this Court and its rejection by the learned District Judge should be overruled.

CONCLUSION

The order of the Court below should be reversed insofar as it pertains to an allowance to the Appellees and in all other respects affirmed.

Respectfully submitted,

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